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May 21, 1998

EX PARTE OR LATE FILED

Magalie Roman Salas
Secretary
Federal Communications Commission
1919 M Street NW -- Room 222
Washington, D.C.

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MAY 21 1998

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Re: **EX PARTE** in Universal Service Reform, CC Docket No. 96-45; Access Reform Tariff Investigation, CC Docket No. 97-250

Dear Ms. Salas:

On May 18, 1998, Michael Pelcovits, MCI's Chief Economist, and I met with Ruth Milkman, James Schlichting, Lisa Gelb, Valerie Yates, and Rich Cameron of the Common Carrier Bureau to discuss universal service contributions for the second half of 1998 and recovery of those contributions from end users. Per the staff's request, MCI has prepared an ex parte to discuss in detail the issues raised.

At the Commission's request, we discussed alternatives to the current line charges on long distance end user bills. MCI noted a May 15, 1998 letter to the Commission from the National Telecommunications and Information Administration (NTIA), expressing the view that the $2.65 billion per year to support subsidies for telecommunications and wiring of schools and libraries, as well as telecommunications discounts for rural health care providers, is equivalent to a $1 per month assessment on every telephone line and every wireless number.

The NTIA's observation, if it were considered as an alternative funding mechanism for schools, libraries, and rural health care providers, would raise a new set of implementation issues that the Commission would need to address prior to adopting such a plan. In the remainder of this letter, we will highlight the implementation issues that MCI believes must be addressed in order that such a change meet its stated objective.

As an initial matter, MCI believes that an explicit charge for universal service recovery is supported by our market research about what customers want. After being read a description of universal service, and being told that all long distance telephone customers help fund universal service obligations, fully 80 percent of those surveyed by Wirthin Worldwide in a national poll said they preferred a separate line item charge on their telephone bills to having a bill that failed to specify this charge. The poll was taken May 1 - 4, and is accurate to within plus or minus 3 percent.

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Current requirements

In the Universal Service Reform Order, the Commission adopted three decisions of particular significance to the current debate. First, it created an explicit set of universal service mechanisms, in some cases changing and expanding funding mechanisms that had existed prior to the Telecommunications Act of 1996:

- High cost fund = $1.7 billion
- Lifeline expanded to $0.5 billion
- Schools and libraries = $2.25 billion (annual cap)
- Rural Health Care = $0.4 billion (annual cap)

MCI notes that in the first wave of schools and libraries applications to be received, requests are estimated to total over $2 billion. Additional applications will continue to be received during the year. However, there is no public information available at this time that would allow us to analyze the "run rate" of monthly payouts to determine whether collection rates are approximately equal to payout rates, less than payout rates, or substantially exceed the payouts under the schools and libraries plan. We believe that understanding this issue would help inform the current debate over contribution amounts, and we will continue to analyze available data to determine if a reasonable estimate can be made.

Second, the Commission decided to allow incumbent local exchange carriers (ILECs) to pass through their universal service contributions to interexchange carriers (IXCs) in the form of higher access charges. As a result, IXCs and their customers pick up a majority of all universal service costs. MCI estimates that IXCs and their customers pay approximately 82 percent of schools, libraries, and rural health care costs, and approximately 95 percent of the High Cost Fund/Lifeline program through direct payments to the fund administrators and indirectly through higher access charges. MCI continues to believe that ILECs should not be permitted to pass along their universal service obligations to long distance carriers.

MCI currently has pending an Emergency Petition in the tariff investigation of the January 1, 1998 rates that would, if granted, require ILECs to itemize for IXCs the amount of universal service contained in our monthly access bills. As MCI has noted, specific information from the ILECs about the amounts of universal service embedded in access charges is required by section 254 of the Act, and would greatly assist IXCs in accurately recovering from our customers universal service assessments.

Third, the Commission gave the IXCs the discretion to recover universal service assessments from their customer base, consistent with the Commission's view that a competitive long distance market should permit different approaches to cost recovery. The Commission did note that one permissible method of recovering universal service costs from subscribers were line charges, and the Commission created some limitations on how IXCs could name those line charges. IXCs have generally created such line charges, and have tariffed a percentage-of-revenues methodology of varying types.

Timing

The Commission has announced its plan to set contribution factors sometime in the next few weeks. As we have previously reported to you, MCI intends to begin charging a universal service fee to our residential customers effective in July, and intends to revise existing universal service fees charged to business customers to collect up to the level of the new contribution factors. MCI has also previously brought to your attention several significant dates that affect our ability to tariff or revise these fees for July, and to explain them to our customers:

June 1 - planned date for interstate tariffing of residential universal service fee

June 8 - the last date for Commission decision on contribution factors that would permit July invoice messaging (contemporaneous with new or revised fees).

Thus, the Commission must establish new contribution factors for the second half of 1998 as soon as possible, and in no event later than the last business day of May 1998 in order for MCI to implement them in July.

MCI offers one further observation about the upcoming deadlines that would permit new universal service contribution factors to be set, or that would permit new recovery mechanisms to be implemented -- there is no legal requirement that the Commission resolve all these issues for a July 1 implementation. MCI urges the Commission to carefully consider whether a brief postponement of the events that lead up to and include July 1 tariff implementation would be beneficial and give the industry sufficient time to implement the latest changes in universal service recovery without adversely affecting the implementation of any Commission policy.

As the Commission is well aware, the date for filing annual access tariffs is a date set by administrative action, and may be moved (and has historically been moved) at the agency's discretion. In addition, the Commission retains the power under section 204 of the Act to suspend tariffs for up to five months. Moreover, it's not clear that increased contribution factors need to be effective as of July 1, 1998 in order to support contemplated payouts from the funds through the second half of 1998. If the Commission is considering changes in its universal service requirements, a brief delay of one month in the collection of universal service subsidies might prove to be beneficial to the Commission without adversely affecting the implementation of any Commission policy.

New Collection Plan for Schools, Libraries, and Rural Health

MCI agrees that a $1 per month assessment on every local loop, local loop equivalent, and wireless number collected by the local exchange carriers, would provide sufficient funding for the Commission's current annual cap on schools, libraries, and rural health care providers. As a rough rule of thumb, MCI estimates approximately 155 million local loops, 23 million special access "loop equivalents", and 50 million wireless "loop equivalents" or numbers. MCI notes that the Commission is about to release a report on wireless subscribership, which should provide more accurate data on which a universal service administrator could calculate contributions owed by particular carriers. In addition, we assume that the Commission would wish to consider the impact of such a charge on lifeline customers, whose financial need is the basis for the reduced charges that they pay.

We note that the problem of how to charge special access loops (called "channel terminations") presents some challenging, but not insurmountable, implementation issues that must be fully considered. Charging $1 per loop equivalent would produce large fees at the DS1 and DS3 level relative to monthly recurring charges for those services today. MCI also notes that a similar issue may be raised with respect to Centrex products. In MCI's view, a per line collection for special access would need to be reduced in certain circumstances (e.g., high capacity) in order to avoid analomous effects. Depending upon the payout rate (noted above), a reduction in collection amounts from special access might not present an under-collection issue with respect to the dollars actually needed to fund subsidies.

As MCI and other IXCs have discovered in trying to recover the Presubscribed Interexchange Carrier Charge, the retail long distance market is not an efficient collection mechanism of fixed monthly fees. Especially for customers of mass markets products, the problem of substantial numbers of customers who do not use service in any given month, coupled with the high costs of billing for those carriers like MCI who use ILEC billing, makes it uneconomic to bill customers for flat charges of $1. As a result, IXCs are likely to have to exceed the $1 per month level in order to collect the full amount of the contribution requirement that they have been assigned. This does not strike us as a good result from either a public policy perspective or from a customer service perspective. Accordingly, the $1 fee cannot be collected by long distance carriers.

Section 254(d) of the Act requires that universal service contributions be distributed among telecommunications carriers on an "equitable and nondiscriminatory" basis. MCI believes that amending the current collection rules to require LEC-collected $1 per month fee for schools, libraries, and rural health care satisfies the legal requirements of the Act. "Equitable and non-discriminatory" should be construed to provide some discretion to fashion universal service mechanisms that treat all similarly-situated carriers uniformily. A LEC-collected and wireless-collected $1 per month fee would not discriminate against any individual exchange carrier or wireless carrier. It is an efficient mechanism, since IXCs are not in the best position to collect such a charge due to zero-use customers. Furthermore, today's system, placing the vast majority of all universal service obligations on IXCs, was apparently not viewed by the Commission as a violation of section 254(d) when the Commission created it.

It is important to note that resolution of issues surrounding the implementation of universal service for schools and libraries and rural health care does not, by itself, alleviate the need of long distance carriers to recover universal service costs. At the current time, long distance carriers are being assessed about $2.2 billion for other universal service obligations, including the present high-cost fund and lifeline services. This includes both the direct assessment on the long distance carriers and the approximately 95 percent of the local companies' obligation which they pass along to the long distance industry in higher access charges.

Finally, any changes in the universal service system should be accompanied by a reduction of interstate access charges. MCI has presented data that demonstrates that, at a minimum, interstate access charges should be cut by $1.8 billion by July 1, 1998. Then, access charges should be brought all the way to cost by January 1, 1999. Until access charges are reduced, a series of false choices will be presented to policymakers: difficulties in the implementation of universal service, delay in the opening of local markets, and disruption of the long distance market. The Commission must now get to the heart of the matter: unjustified access charges.

Sincerely,

Mary L. Brown

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CC: James Schlichting
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